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IN THE

Supreme Court of the United States

October Term, 1977

No. 77-107

WESTERN PHARMACAL COMPANY,
a Utah corporation,

Petitioner,

v.

AMFAC DISTRIBUTING CORPORATION,
a California corporation, dba
WESTERN DRUG SUPPLY CO.,

Respondent.

BRIEF IN REPLY TO OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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Pursuant to Rule 24, Supreme Court Rules, Petitioner, Western Pharmacal Co., replies herewith to arguments first raised in Respondent's Brief in Opposition to Petition for Writ of Certiorari.

In its statements of facts, Respondent, Amfac Distribution Corporation, makes two statements of fact which are misleading and prejudicial:

1. Respondent asserts that upon remand after the first appeal, "the District Court, without further evidentiary hearing or accounting, awarded Petitioner the sum

of $144,000.00 which purported to be Respondent's profits during the period of infringement. The Court of Appeals again reversed, saying that it would be 'unconscionable' . . . and again remanded the case for an evidentiary hearing . . ."

The correct statement of this part of the case is: On remand after the first appeal, the District Court ordered (1) the Respondent to pay to Petitioner the amount of profits shown in Respondent's initial accounting for the infringement period up to July 9, 1973 (which, incidentally, showed a profit — before income taxes — of $400,702.00) and (2) to supply a supplemental accounting for the infringement period after July 9, 1973. [The District Court's order to pay the entire profits accounted for was premised on the fact that Respondent had not adduced any evidence at the trial as to what portion of such profits were not attributable to the infringement nor had the Respondent requested a severance at the time of trial in order to present its evidence of "profits not attributable to the infringement" at a separate hearing.] The Court of Appeals by its second mandate did not reverse the "accounting," it merely afforded Respondent a separate hearing on profits including a right to submit proof as to what portion of its profits were not attributable to its infringement.

2. Respondent says next in its statement of facts, "after denying Respondent the opportunity to take any discovery the District Court held a hearing on February 19 and 20, 1976 . . ."

The fact is that Respondent had its discovery. After Respondent was denied "its discovery" (i.e. the District Court had ruled that Petitioner was not required to respond to certain Interrogatories and Requests for Admission served on Petitioner by Respondent) Respondent petitioned the Court of Appeals for a Writ of Mandamus calculated to force a response to said Interrogatories and Requests. Because it appeared to Petitioner that the Mandamus proceeding would result in further delays including loss of the February hearing date, Petitioner voluntarily *supplied* the requested discovery, the Petition for Mandamus was denied, and the hearing was held as scheduled.

1. *Does the Petition Present a Question Appropriate for Review?*

Respondent argues, for the first time in this protracted litigation, that a federal question is not involved. Respondent says the case involves "only common law trademark . . . questions . . . calling into play only the laws of [Utah]."

This position is highly inconsistent with the stance taken by Petitioner throughout this litigation and up to the filing of its Opposition Brief.

Respondent has repeatedly relied on this Court's ruling in *Mishawaka Rubber & Woolen Mfg. Co. v. S. S. Kresge Co.*, 316 U.S. 203, 86 L. Ed. 1381, 62 S. Ct. 1022 (1941). Indeed, it was Respondent who first brought this case to the attention of Petitioner in its Motion to Amend the Judgment of the District Court. Respondent relied almost entirely on *Mishawaka* in its second appeal. In that appeal, Respondent sought and obtained a ruling by the Tenth Circuit, which ruling was based on *Mishawaka*, that Respondent would be permitted to introduce evidence as to what portion of its profits were not attributable to its infringement of Petitioner's trademark.

Petitioner's trademark was earlier federally registered and the Registration inadvertently not renewed. The Registration has been re-acquired. The effect of the lapse of the Registration on this lawsuit was not litigated below and is not at issue here.

2. *Did Petitioner Contend that Mishawaka Requires that an Infringer's Profits be Turned Over to a Trademark Owner in Every Infringement Case?*

Respondent postulated that Petitioner did so contend and then proceeded to show the contrary in order to meet Petitioner's argument that the Tenth Circuit did not follow *Mishawaka.*

This Court's opinion in *Mishawaka* specifically said that no issue was involved as to when or under what conditions an infringer's profits may be awarded to the trademark owner. It is true that the dissent in that case was preoccupied with this question. But the majority opinion presumed that the *award* of profits had been properly made and further supposed that *all* of the infringer's profits did not result from the infringement. The opinion then dealt solely with the issue as to whether the trademark owner would be required to show what portion of the infringer's profits were attributable to the infringement or whether the infringer would be required to show what portion of the infringer's profits were not attributable to the infringement. The decision, of course, adopted the second alternative.

Petitioner agrees with Respondent that *Miskawaka* does not require *an award* of profits in every case because it was not concerned with the issue. But where an award of profits has been made, where the trademark owner meets his burden to prove gross sales and where the infringer fails to meet his burden to prove business expenses so as to arrive at the net profit or where the infringer fails to meet his burden to prove what portion of its profits are not attributable to the infringement, *Mishawaka* does require that the amount proved by the trademark owner shall be awarded except as decreased by the proofs of the infringer as to business expenses and as to the portion of profits not attributable to the infringement — even if such award amounts to a windfall. And this is the *Mishawaka* rule which the Tenth Circuit first followed and later refused to follow.

3. *Was the Question of Whether Profits should be Awarded to Petitioner Reserved Until Completion of the Hearing on Profits?*

Respondent suggests, for the first time, that the question should be answered in the affirmative, citing *Obear-Nester Glass Co. v. United Drug Co.,* 149 F. 2d 671, 673 (8 Cir. 1945). However, that case supports Petitioner, not Respondent. It was there held that an opinion of the Court of Appeals in a prior (interlocutory) appeal which determined (1) that there had been an infringement of a valid trademark, (2) that the infringement was willful, and (3) that the appellant was entitled to an accounting of appellee's profits and damages was the law of the case. Then the Court said, "the effect of that (interlocutory) decision was not to determine in advance of the accounting, that appellant was entitled to recover either profits or damages *in a substantial amount.*" (Emphasis added). That is, proofs must be offered to show the *amount* of the recovery of damages and profits. Thus the only question reserved for completion of the hearing on profits and damages was the *amount* to be recovered. The Court, quoting *Mishawaka,* then proceeded to discuss

the proofs that would be involved in determining the amount of the recovery. It also discussed the burden of proof imposed by *Mishawaka*.

In the case at bar, a reading of the second mandate of the Tenth Circuit disposes of the question in the negative. It is completely clear from that opinion that an award of profits had been made by the District Court, that the award had been approved by the Tenth Circuit, and that the *only* issues remaining in the case respecting profits was to determine, as in *Obear* the amount of the profits and the portion of that amount attributable to the infringement.

The course of the hearing on profits and damages was set by the following language from the Tenth Circuit's second mandate:

1. Petitioner shall be "permitted to . . . put on proof of its actual damage."

2. On remand, Petitioner is entitled "to those profits attributable to [Respondent's] infringement of [Petitioner's] trade name."

3. "If [Respondent] affirmatively demonstrates that some of its Utah profits are not attributable to its infringement [the same may be used] as an offset to its total gross profits."

4. "We emphasize the burden of proof is on [Respondent] to clearly demonstrate that the profits it has enjoyed during the period of infringement are not attributable to the unlawful use of [Petitioner's] name."

5. The cases of *Mishawaka*, supra, and *Blue Bell Co. v. Frontier Oil Refining Co.*, 213 F.2d 354 (10th Cir. 1954) are to control Petitioner's recovery of profits in this case.

6. Those cases provide that (1) Petitioner has the burden of proving Respondent's gross sales, (2) Respondent has the burden of proving operating expenses to arrive at net profits, and (3) Respondent has the burden of proving what portion of the profits are not attributable to the infringement.

Pursuant to the second mandate:

1. Petitioner submitted proof by a qualified expert witness that its plans for expansion could not be implemented because of the economic burden placed on Petitioner to purge Respondent's infringement. The qualifications of Plaintiff's expert were not questioned and his opinions were not discredited either by cross-examination or contrary evidence. Petitioner's proof was consistent with the Tenth Circuit and U.S. Supreme Court authorities cited in the original Petition for Certiorari. Said proof consisted of (a) proof of losses sustained during the infringement period — 1971 through August 15, 1974 — of $164,510.00, (b) proof of loss of profits of $93,372.00 during the same period in consequence of Petitioner being unable (because of the financial burden imposed on Petitioner by Respondent) to implement its plans for expansion, and (c) loss of profits of $223,754.00 during the "turn around" period involved in recovering from the financial burden.

2. Petitioner met its burden to prove Respondent's gross sales — of over $18,000,000 — via a stipulation filed with the District Court.

3. Respondent met its burden to prove cost of goods sold via the same stipulation, resulting in an established gross profit of $2,267,353. In order to arrive at the net profit, Respondent next proceeded to submit proof of operating expenses.

4. Respondent attempted to prove "administrative costs" of $179,118.00 and their deductibility from the gross profits. Respondent's attempt failed because it was admitted that most of the expense was that of a non-party parent corporation and because no direct testimony or documentary evidence was offered to show that such costs were the actual expenses of Respondent.

5. Respondent attempted to prove the deductibility of "branch expenses" in the amount of $1,635,354. However, Petitioner offered no direct testimony or documentary evidence breaking such amount down into categories so that the deductibility of each category could be demonstrated. Adequate authorities were cited to show that such was required.

6. Respondent's attempt to establish its income taxes of $215,819.00 as a deductible expense was defeated on the ground that, under authorities, income taxes are not a deductible item where the infringement was deliberate, as here.

7. Respondent attempted to prove deductibility of $48,311.00 in interest expense allocated from the parent corporation. This item was disallowed because it was an expense of a corporation not a party and because no direct testimony or documentary evidence was offered to show it was an actual expense of Respondent.

8. Respondent attempted to prove the deductibility of $67,178.00 as branch interest expense. This item was disallowed because it was admitted by Respondent that the interest was paid on obligations incurred prior to the infringement.

The Tenth Circuit — (a) after devoting its second mandate to delineating the course that the hearing on the amount of profits and damages to be awarded was to follow, (b) after placing the burden on Respondent to prove offset, (c) on being faced with the almost total failure of Respondent to prove offset, and (d) on being faced with the almost total failure of Respondent to meet that burden — did not even review the strength or weaknesses of Respondent's proofs.

Instead, it arbitrarily, on its own motion, and without any new evidence on the issue reversed its position taken in the second mandate on the issue of whether profits should have been awarded in the first instance. And it rejected Petitioner's proof of damages, founded on prior holdings of the Tenth Circuit, without any attempt to distinguish the case sub judice from those holdings.

4. *Did Equitable Factors Favoring Respondent Appear for the First Time at the Hearing on Damages and Profits which Justified a Finding that Respondent's Infringement was not Sufficiently Serious to Justify the District Court's Award of Profits?*

The Tenth Circuit's third mandate said "yes," claiming that such hearing first made it manifest that Petitioner had not (1) lost any sales intended for Respondent, (2) sustained any damage to its reputation, and (3) made any claim that Respondent palmed off its goods as those of Petitioner. Petitioner has already noted that proof at

the original trial had established each of these propositions. None of them surfaced for the first time at the hearing on damages and profits. That hearing did not present "a materially different situation" on these issues — as contended by Respondent. Profits had been awarded on the basis of Respondent's willful infringement.

The Court of Appeals made this observation in its second mandate. It said, "The award of profits . . . was intended to render deliberate trademark infringement unprofitable." And, *Respondent "was not an unwitting infringer, it deliberately used* [Petitioner's] *name, knowing full well the consequences of its acts."* (Emphasis added.) One Court has said that "where the infringement was deliberate and willful . . . both the trademark owner and the buying public are slighted" unless recovery includes an award of profits. *Maier Brewing Co. v. Fleishman Distilling Corp.*, 390 F.2d 117 123-4 (9th Cir. 1968).

The District Court's award of Respondent's profits was not based on the extent of the damage to Petitioner and, according to *Maier,* supra, need not be. However, the extent of Petitioner's damage did become substantial as a result of Respondent's willful infringement and vengeful prolongation of the infringement litigation.

It is of considerable importance to note that in the three appeals — all taken by Respondent — Respondent did not once raise the question of whether the award of profits had been properly made.

The only new factors disclosed at the hearing on damages and profits were (1) the extent of damage sustained by Petitioner as a result of Respondent's willful prolongation of the infringement litigation, (2) Petitioner met its burden, by stipulation, to prove Respondent's gross sales,

(3) Respondent met its burden, by the same stipulation, to prove the cost of goods sold, (4) Respondent did not meet its burden to prove deductibility of alleged operating expenses, and (5) the proof showed that Respondent's profits during the infringement period were all attributable to use of the infringing name, "WESTERN DRUG." These factors have no bearing on the question of whether damages and profits should have been awarded in the first instance; they bear only on the *amount* of damages and profits to be recovered.

5. *Was the Cost of Prosecuting the Infringement Action a Proper Element of Damage?*

Petitioner acknowledges that attorneys fees are often awarded as an element of damage. However, Petitioner has shown that attorneys fees are justified in this case. *Clifford Vaughn v. N. J. Atkinson etc. et al,* 369 U.S. 527, 8 L. Ed. 2d 88, 82 S. Ct. 997, reh. den. 370 U.S. 965, 8 L. Ed. 834, 82 S. Ct. 1578 (1962). Respondent made no attempt to show that the case sub judice does not fall within the rule of *Vaughn.*

6. *Was the Judgment of the District Court Contrary to the Tenth Circuit's warning against "a truly harsh result?"*

Respondent argues in the affirmative.

The Tenth Circuit established the meaning of this phrase in its second mandate: "The rule that profits not attributable to the infringement be denied was an important corollary to the principle of awarding profits so that the courts could avoid 'a truly harsh result.'" Thus, if the infringer is afforded opportunity to submit proofs of what portion of its profits are not attributable to the in-

fringement, it is presumed that the infringer must make use of that opportunity and will offer such proof, thereby avoiding "a truly harsh result." As noted above, the Court said "we emphasize [relying on *Mishawaka*] that the burden of proof is on [Respondent] to clearly demonstrate that the profits it has enjoyed during the period of infringement are not attributable to the unlawful use of [Petitioner's] name." Thus the second mandate, applying *Mishawaka*, provided the infringer with the *opportunity* to avoid a "truly harsh result," but the burden was on the infringer to avoid such result. When Respondent failed in that proof, the Tenth Circuit [now absent the influence of Justice Tom Clark (who had ably written the first two opinions)] exhibited prejudice against the District Judge and equated "a truly harsh result" with the windfall contemplated (and mandated) by *Mishawaka*. To the contrary, where an infringer fails to its proof, *Mishawaka* should continue to apply.

CONCLUSION

Thus, in an effort to contend with the Trial Judge, the Tenth Circuit has undertaken to overrule the United States Supreme Court (in *Mishawaka*). Accordingly, the Petition for Writ of Certiorari should issue.

Respectfully submitted,

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